Emergence of Managerial Capitalism in India

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Abstract: The present paper aims at analyzing whether and to what extent Alfred Chandler’s managerial capitalism as he defined it, appeared and controlled the industrial development of India. An attempt has been made to trace the development of Indian industries during the British rule, the problems faced by the early entrepreneurs and finally the managerial system adopted by them for the continued expansion of their industries. This is then compared to A. Chandler’s concept of managerial capitalism and some conclusions/hypothesis formed.

I. INTRODUCTION

Rise of capitalism marked the end of unhealthy restrictions and controls over trade and beginning with Adam Smith, the classical and neo-classical economists strongly defended the principle of Laissez faire. They felt that the invisible hand of the market mechanism, if left to itself, was sure to establish fair competition among the sellers. Through this it was believed that a just and equitable system of production and distribution would be assured under which everyone would get what the deserved, i.e. his marginal productivity, and there would be no exploitation in the long run. Like God, the invisible hand was controlled by none and (if its rules were strictly followed) did justice to all. Laissez Faire, or leaving all economic activity to the free play of the invisible hand (market mechanism) became the sine-quo-non of the entire capitalist socio-economic philosophy. However, even under the so called capitalist economic systems the market mechanism was never entirely free. Under the guise of preventing monopoly labour unions were banned, though employees associations existed. In other words, the rules of the game of Laissez Faire were followed by its exponents only so far as they were suitable to them.

During the latter half of the nineteenth century, as the effects of industrial revolution came to be felt, the market expanded from local to national, due no doubt to the introduction of railroad, telegraph, telephones, etc., which led to improved transportation and communications. The cumulative effect of these factors along with improved technology brought about a revolution in marketing. Commission agents were pushed aside by commodity dealers and wholesalers who in turn were supplanted by retailers. These expanding market horizons necessitated the establishment of branch houses or units in order to capture larger market shares by producers. Backward and forward integration of business houses followed to ensure a steady supply of raw material and demand for products. The form of business that emerged as a result was that of multifunctional multiunit enterprise.

Industrial output soared with integrated production and mass distribution. Entrepreneurs, in order to maximize profits, either tried to control sources to avoid competition or added new units to ensure the benefits of economies of scale. Large integrated enterprises with multiple function and working over a large area had greater potential for expansion. With their extensive marketing, manufacturing, purchasing, raw material sources, transportation and research and development facilities, these entrepreneurs found it difficult to manage the enterprise effectively. This led to the emergence of managerial capitalism.

With the increase in size of industrial enterprises, a tendency towards the separation of ownership and management became apparent. A class of professionals, who were not necessarily from the traditional business families, developed to take over the management of these enterprises. Unlike the market mechanisms which were invisible and directly uncontrollable, this class of professional managers, who controlled the working of the giant industrial enterprises and also influenced at times the market mechanism, was visible. Hence Alfred Chandler refers to them as “The Visible Hand”. He states that up to the end of nineteenth century financial or family capitalism was present in the American economic system where the entrepreneurs had the ultimate say in business decisions. By 1917 however, they were rarely involved in the decision making process and never negatived the decisions of managers with respect to prices, output, deliveries, wages or employment. From his study of over 200 non-financial American companies in 1963, he concludes that in none of them any family held more than 80% shares and 50% control by these families existed in only 5 companies. In fact 169 or 84.5% of these companies were management controlled. In short he concluded that managerial capitalism gained ascendancy over family and financial capitalism in the modern multiunit enterprises in America.

Alfred Chandler refers to Managerial Capitalism as “a new type of capitalism- one in which the decisions about current operations, employment, output, and the allocation of resources for future operations were made by salaried managers who were not owners of the enterprise”.

Reasons for the emergence of managerial capitalism as given by A. Chandler can be summarized as under:-

1. Multiunit business enterprise replaced small traditional enterprise when administrative coordination permitted greater productivity, lower costs and higher profits than coordination by market mechanisms.
2. As the activities of many business units were internalized within a single enterprise, a managerial hierarchy had to be created.
3. Volume of economic activity reached a level that made administrative coordination more efficient and profitable than market coordination.
4. Once a managerial hierarchy had been formed it became a source of permanence, power and continued growth.
5. The career of salaried managers who directed these hierarchies became increasingly technical and professional.
6. As the enterprise grew and its managers became more professional, the management became separated from ownership.
7. These career managers preferred long term stability for maximizing current profits.

**Need and Objective of the Study**

As per Chandler’s definition the Visible Hand was a class of professionals developed to take over the management of traditional family businesses. Another term coined for this class of professionals was Managerial Capitalism. The need was felt to trace the development of this in India.

In order to determine the managerial system prevalent in India it was necessary to study its economic development and impact of religion, culture and society on industrial development. Based on this the objective framed for the present research was to study the emergence of Managerial Capitalism in India and determine whether the managing agency system in India could be equated to the same.

**II. RESEARCH METHODOLOGY**

The present research is descriptive in nature and because it is an attempt to trace the emergence of Managerial Capitalism in India, it is a historical study of various developments and factors influencing those developments. As such the methodology adopted is secondary in nature, involving review of literature of industrial development during the 19th and early 20th century. A study of the evolution of the managing agency system was also necessary in order to conclude whether it could lay claim to being known as India’s Managerial Capitalism.

The present paper aims at analyzing whether and to what extent Chandler’s managerial capitalism as he defined it, appeared and controlled the industrial development of India. An attempt has been made to trace the development of Indian industries during the British rule, the problems faced by the entrepreneurs and finally the managerial system adopted by them for the continued expansion of their industries. This is then compared to Chandler’s management capitalism and some conclusions/hypothesis formed.

**Economic Development of India**

India of the pre-British period possessed a feeble transport system because as a result of scientific & technical backwardness of people modern industries which could manufacture modern means of transport did not exist. A weak economy perpetuated weak transport which hindered development of that economy. Traditionally there existed what is known as the self-sufficient village economy. The village looked to the outside world for little more than its salt, spices, the fine cloth for holiday clothes and the coin in which it paid its revenue. Uniform price structure was unknown.

In the first half of the 19th century, powerful machine based industries sprang up in England and the industrialists were faced with problems of procuring raw material and disposing of products. They urged the Government of East India Co. to establish railways and construct roads. Britain had accumulated capital which could not be profitably employed in Britain. If the Indian Government constructed railways, it needed capital which Britain could loan and thus find a profitable outlet. Coupled with this, there were political, administrative and militarily strategic reasons for establishing railways in India. Thus modern means of transport were established to primarily serve the economic, political and military interests of Britain in India. Railways helped build a national economy. They made inevitable the birth of Indian industry owned by Indian capital whose very interests brought them into conflict with Britain. One significant result of British conquest was the establishment of a centralized state which brought about a real and basic political and administrative unification of the country.

Unification also brought its attendant problems. The internal custom barriers in the shape of Transit and Town duties rendered free entry to the market impossible. The manufacturer had to pay duty twice on raw material and finished products. This led to rise in cost of production. In consequence Indian goods could not stand in competition with foreign machine products even within the country. Tariff legislation is a matter of vital importance to initial economic development of a country. With the employment of machines in methods of production, the volume of commerce must grow and it is necessary that it should be regulated in a manner beneficial to the manufacturing interests of the country. Upto 1846, however, there was no single tariff plan for the whole country. Custom duties were collected in the Presidencies according to different principles. It seemed the government was primarily anxious to safeguard the English commercial interests in India and acted accordingly.

While reforming the policy of commercial taxation in India, the ground was prepared for deep penetration of industrial capitalism of England. The Government of India and Secretary of State took shelter behind the facade of Free Trade. As R.C. Dutt remarked, “the ultimate tendency of free trade communities with different standards of living is to reduce these standards to a common level.” However, free trade as applied to India was a one way affair. It granted freedom of trade to England against India. To quote Mr. JamesInglis (1882 Legislative Council of India) “Free trade is all very well and at the right time and place an excellent thing. But babies cannot digest strong meat and for India in her half
developed semidormant state some of the theories of political economists are very stringy salt junk"

According to T.S. Banerjee free trade was imposed on an unwilling India under political pressure. He quotes Dadabhai Naoroji "Free trade between England and India was something like a race between a starving exhausted invalid and a strong man with a horse to ride on." Fraternity was emphasized, equality preached but no real sympathy for economically resurging India was forthcoming. The attempts of the British in India have often been said to have originated from a motive of exploitation. However, while it is true that England was prompted by self-interest when she carried out economic reforms, there is no denying the fact that India benefitted indirectly through unsought consequence of British decisions and acts.

Impact of Religion Culture and Society on Industrial Development

The Caste System in India had led to occupational immobility. In ancient and medieval India, the occupational division among Hindus was intact. Commercial activities were a monopoly of the Vaisyas and there was nothing to suggest that members of the other three Hindu Varnas - Brahman, Kshatriya and Shudra were ever drawn into trade and commerce. The beginning of European commercial enterprise in India in 1600 did not substantially disturb the degree of occupational basis of Indian society nor did it effect any qualitative change in the activities of the commercial classes.

D. Tripathi states that the traditional mercantile class dominated business and commercial activities almost till the onset of 19th century, they introduced no qualitative change in business practice and remained unduly wedded to liquidity preference. The chief commercial and trading communities were inhibited by their religious traditions to innovate and experiment. It is in this context that Best Hozelitz wrote "Industrial entrepreneurship can be developed in a society in which cultural norms permit variability in the choice of paths of life and in which relevant processes of socialization of the individual are not completely standardized and demanding conformity to a prescribed pattern." Unfortunately during the 18th and early 19th century, the cultural norms of Hindu society provided little choice in the paths of life; on the other hand the individual was compelled to conform to a set pattern of life.

After 1757, the operation of British free merchants was facilitated and business horizons expanded. The Agency houses played an innovative role. They were set up originally to facilitate remittances to England but soon entered trade and commerce and added lines such as banking and shipping. Such houses increased and activities expanded after 1813 when East India Company lost its monopoly. They financed and promoted plantations, participated in risky business of coal mining, established leather manufacturing, etc. During this period, material changes were taking place in the social and cultural fabric e.g. spread of western ideas, secular education, loosening grip of religious & traditional ideas and encouragement to non-mercantile classes to look at opportunities for gain e.g. high caste Brahmins like Dwarkanath Tagore, R.M. Banerjee and Prasana Kumar Tagore. Between 1834 and 1847 numerous Indo-British partnerships were begun though most had disappeared by 1847. The activities of British entrepreneurs gave Indians a form of corporate management, brought them face to face with superior technology and availability of personnel. During this period, the spread of western ideas and secularization of education made considerable progress.

The beginning of modern factory system in India can be traced to 1850-51 through sporadic and isolated attempts to set up factories were made earlier. The pioneering efforts were made by two communities of Western India - the Gujrati speaking Hindus and the Parsees who had migrated to India from Iran. The first modern cotton mill was started by a Parsee Dadasaheb Damji in 1851. The first Hindu to set up a cotton textile mill was a Nagara Brahmin Ranchodlal Chhotelal in 1858 in Ahmedabad. These two pioneers set in motion the development of the cotton textile industry in India. In spite of British opposition, the cotton industry was firmly established by 1875. The British had introduced railways in India primarily to serve their defense needs. However, this had an impact on the growth of Indian industry. The pioneering role was played by Parsees on account of their exposure to the new ideas and values of the British for whom they acted as agents.

Cotton textile mills were established by Indian entrepreneurs in Kanpur, Madras and Nagpur in the 19th century. The jute industry also adopted the modern factory method. Though the first jute mill was set up by a Scotsman in the Hoogly region, Hindu entrepreneurs soon followed suit. J.N.Tata, a Parsee from a priestly family, set up three cotton textile mills and was the first to divert his resources into heavy industry - iron and steel, despite lack of government support. Indian entrepreneurs gradually extended their enterprises to sugar, matches, cement and coal industries. The sugar industry began in Calcutta in 1875, progress was slow till 1930 after which within a period of four years, the number of factories increased from 31 to 111. Tatas set up the first cement factory in 1912 and by 1925 there were ten companies in this industry.

The Parsees and Gujarati Hindus were followed by the Cheltrais of the South and Marwaris of Rajasthan. We have several examples of individual entrepreneurs coming from various communities and castes in India who pioneered a number of industries despite traditional restrictions on the role of their communities. Birlas came onto the industrial scene after the first world war. The traditional business and trading communities like Bamas of Gujrat and Marwaris of Rajasthan stepped into industrial activities in an organized and big way. The rise of Marwaris is a vivid illustration of the capacity of this community to adopt its traditional methods of business to the demands of modern industrial enterprise. This community...
with its tenacity of purpose and willingness to take risk, with its sharp insight into business as well as a strong sense of solidarity made itself one of the most prosperous communities in India. These traditional business communities however, had lagged behind the entrepreneurial initiative throughout the 19th century. This hesitation to enter into non-traditional risky ventures may be explained by the educational and environmental factors.

The infrastructural changes and more particularly the demands for indigenous products created during the second world war led to the emergence of new opportunities. Consequently, by the time of independence, religious inhibitions against business had been considerably weakened, the backbone of occupational immobility had been broken and outlook of so called business communities had broadened.

One aspect of social organization in India deserves some study - the joint family system, which had a bearing on economic development. In the west the concept of family is that of a nuclear family, where the children live their separate lives and plan out their course of action according to their abilities and choices. India, on the other hand, has the joint Hindu family system where the members - consisting typically of the head of the family and his wife, their sons and daughters-in-law and a number of grandchildren pool their earnings and are maintained out of the common fund. The advantage is that the blows of fortune, are borne by the group, not the individual, so that there is no need for organized poor relief except in times of famine. The disadvantage is that both personal ambition and the span of need are lacking, and therefore, the incentive to effort is very slight. The authority of the head of the family gives additional weight to the forces of conservatism, preventing initiative and hindering social and economic changes. Any person who leaves his home in order to take up work in a town does not burn his boats. He goes to town with the express object of earning money and then returning to his inherited plot of land. The businessman, instead of reinvesting his profits in his own business or branching out in some new line, shares the proceeds with his brothers and sisters, brothers and sisters-in-law, nieces and nephews, to say nothing of his parents, grandparents, uncles and aunts. If a man loses his job, he is not obliged to take another, but can live with his wife and children on the income earned by a more successful relative. It is this, in fact which enabled industrial workers to withhold their labour from the market, in spite of great poverty. Under such a system the head of the family controlled the purse, exercised undisputed authority over junior members and had a decisive vote in matters affecting the family. This system as will be seen later played an important role in the development of a managerial system by early Indian entrepreneurs.

Emergence of Managerial Capitalism in India

Upto1834, the English East India Company pursued a policy of keeping other Europeans away from India. It also discouraged local merchants from the north as also those who engaged in exports. As a result of this policy, much of the free private trade passed into the hands of British servants of the Company and some "free merchants". A free merchant was one who was permitted by the Company to enter a Presidency in India and trade there under license. At a later stage, when Company servants were prevented from taking part in private trade, they obtained permission to resign and engaged in agency and commercial business. Thus a substantial portion of private trade came to be concentrated in the hands of a few agency houses, which were partnership concerns and which became the characteristic units of private British trade. The agency house was simply a merchant dealing in various articles on behalf of the parent companies at home at a commission e.g., insurance, shipping, etc. They were the bankers of the non-trading European community in India. However, during the depression of the 1830's most of these agencies disappeared. Around this time, the managing agency system had originated. History, geography and economics have combined to create and develop the managing agency system. Its origins can be traced to the social and economic conditions which prevailed in India at the time when monopoly of trade was lost to the East India Company. At that time India offered plenty of opportunities to enterprising businessmen. There were however obstacles in the way of exploiting such opportunities viz. (1) shortage of entrepreneurship, (2) dearth of venture capital, and (3) lack of technical and managerial know-how. The managing agency system was evolved to meet this challenge. Blair B. Kling in his article on the origin of managing agency system dates its beginning as 1836 when Carr, Tagore and Company were appointed the managing agents of the Steam Tug Association. R.S. Rougta disagrees with this. The origin of managing agency system is obscure. What is acceptable is that it literally rose on the ashes of the old agency houses.

The government recognized the right of the Europeans to own land and this led to the introduction of plantations and coal mining (Alexander & Co.). The development of British merchants with links in England were naturally inclined to expand their activities by utilizing such resources as were readily available for exports and hence the main interest of British managing agency houses originally was in the export and extractive industries - hence development of jute industry, plantations and mining.

The same conditions were responsible for growth of Indian managing agency firms. The more enterprising Indian businessmen (nearly always from non-traditional mercantile communities) turned to trade and accumulated large funds which they invested in industrial ventures. The agency system was found to be an excellent framework within which business ability could be best developed and limited finance put to best possible use. While British firms took mainly to export and extractive industries, the Indian houses (particularly in Bombay and Ahmedabad) followed a more conservative course and took to consumer goods - usually all began with cotton textile manufacturing.
The Swadeshi Movement of 1906 gave impetus to development of Indian houses and the boom after first world war gave scope for their branching out in new spheres. At this stage, the house of Tatas appeared on the industrial scene in a big way and, unlike their counterparts who confined their promotional activities to proven paths, made an unconventional and successful bid in the field of heavy industry. To them goes the credit of founding the iron and steel and hydro-electrical industries.

The managing agency system may be defined as an institutional development of industrial organization where the promotion, finance and administration of a vast agglomeration of miscellaneous and unrelated enterprises, viz., mines, plantations, mills, public utilities, shipping interests, sales agencies and investment trusts are controlled by a single individual, partnership, private or public limited company. The managing agency houses during 1850 to 1956 constituted the principal foci of decision making. Under this system several companies, though separate and independent legal entities, were controlled by a single family. The modus operandi was simple. A family with some financial strength would launch a company and allot to its own members or near relatives sufficient number of shares necessary to control the new concern. Simultaneously, those holding the controlling interests joined to form a managing agency firm - usually a partnership or sole proprietorship - to which the management of the new company was entrusted under an agreement stipulating the terms and conditions between the managed company and the managing firm. Thus technically speaking, the managing agents did not own the company; they only managed it for which they were remunerated. Managing agency is the bone around which the flesh and sinews of Indian industry have grown. G.W. Tyson in 1953 wrote "In a country where the banking system was neither very developed nor pervasive, where a well organized capital market did not exist and where the geographical factor of long distances from ports to centres of production were the characteristic features, the contacts which enabled Indian industry and trade to take advantage of a rapidly expanding world trade were supplied by the managing agents.

The benefits of group management and organization, of specialist and technical services which a single mill, mine or tea garden could not afford were also secured under the system.”

The role of pioneering enterprises and the subsequent linking up of their interests with the success of the new concerns were regarded by P.S. Lokanathan as the historical characteristics of the managing agents. The success and efficiency of the system were traced to administrative integration, consistent financial aid and continuity of interest. The managing agency system was introduced in India by European entrepreneurs who were reluctant to come here to set up business and manage it. It was a devise by which British investors invested in shares of a managing agency which in turn controlled several industries. Indian entrepreneurs soon followed suit.

The Indian agencies were formed by three or four families banding together with the sole purpose of promoting business enterprise. Among the early leading Indian agencies were Tata & Sons (1887) and Currimbhoy Ebrahim & Sons Ltd.

The main functions involved in the formation and operation of a business may be classified under three heads - promotion, financing and management. These were highly specialized in industrially advanced countries with the setting up of professional promoters and specialized financing institutions. However, in India the managing agency has been connected with these aspects. During the growth of this system when there were few industrial entrepreneurs and no facilities of a capital market, these functions were more or less dependent upon important national industries, viz., jute, cotton, textiles, tea, coal, iron & steel.

Managing agencies operated in much the same way as holding or investment companies operate in the West. Using the first company as a base, the managing agents could float a series of companies cutting across various sectors of the economy. The managing agents did not have to acquire controlling shares in the subsequent flotations as the older companies controlled by them could acquire controlling interests to ensure that the management of the latter concerns did not go out of their hands. Through such a process, managing agents created their business empires. A number of companies controlled by a particular family - directly or indirectly, constituted a business group or house, known generally by the name of the family that controlled the managing agency. D. Tripathi and M.J.Metha state that the growth of industrial entrepreneurship in India during 1850-1956 was due to the entrepreneurial initiative and continuum on the part of these houses, as very few companies remained outside the rubric of the managing agency system.

An analysis of the main interests of top managing agency houses up to 1957 substantiates that they had varied (but to some extent specialized) industrial interests. The Andrew Yules was particularly interested in tea, coal and jute; Birds in coal mining, paper, jute spinning and weaving, iron and steel; Meleods - tea, jute and railways; Birla’s - cotton, jute and other textile mills, paper and tea; Duncans- tea, jute, pressing and manufacturing; Karam; Chand Thapars- coal, sugar, wholesale trade and paper; Octavius Steel - tea plantations and electric under-takings; Martin Buru - railway transport, cement, iron & steel and electric supply; Tatas- iron & steel, hydro-electric power, cotton and oil mills, chemicals, transport and till 1950 airlines. This diversification of interests secured distribution of risk involved in investments while specialization was conducive to the acquisition of specialized technical knowledge and experience. Such a varied interest also led to horizontal and vertical integration which in turn resulted in security to a number of industries.

As stated earlier, the managing agents fulfilled three important functions in the industrial economy of India - entrepreneurial, financiers and business managers. As entrepreneurs they had
taken upon themselves all the risks and responsibilities of pioneering new industries in a country where industrial development had scarcely been significant. They were suppliers of finance by - subscribing to the share capital and debenture issue of companies or getting them subscribed by friends, relatives or other companies; underwriting issues; arranging loans from banks & pledging their guarantees for the same; attracting deposits from the public on the strength of their reputation and standing in the business world; and making advances to the companies out of their own private resources. The latter three were specially so in case of companies having long gestation periods. In fact, the supreme achievement of the managing agency system has been to draw Indian capital away from its traditional preference for land investments into the field of industrial participation.

The managing agency system came to occupy a prominent place in the field of industrial promotion and management in India. For their services they were remunerated through commission of sales, profit, purchases, office expenses, agencies etc. In spite of this and the fact that these agency houses were family owned, technically there was a divorce between ownership and management. R.K. Hazari’s study (1956) supports this contention. He shows that the ownership of managing agencies in the managed companies is negligible - except in unusual circumstances when investors were not forthcoming. People came to possess a kind of blind faith in enterprises managed by managing agencies and were generally doubtful about the success of industrial units not promoted or managed by them.

III. CONCLUSIONS

Having analyzed the origin and functioning of the managing agency system one can conclude that before 1850 most of the businesses in India were sole proprietorships. The managing agency was conceived as a manager company in relation to other ventures by the British investors who were not prepared to come to India or to stay here after retirement. In addition, some of the reasons which facilitated the consolidation of the managing agencies were:-

1. The existence of a limited number of individuals who had the ability and willingness to invest in industrial ventures. The caste system with its Vaishya businessmen did not look kindly towards industry. The traditional mercantile class was hesitant to leave the sheltered arena of money lending and trading for the risky & new fields. This led to a shortage of entrepreneurs which obviously resulted in strengthening of the managing agencies.

2. Even if people were prepared to take the risk of going into industry, they lacked the resources to do so. With a tight and infant capital market only those who had proved their worth or those who had the funds could think of establishing an industry. A managing agency which had successfully promoted and managed a firm was therefore encouraged.

3. The managing agency was in conformity with the social system, viz., the joint family system. It was nothing but the extension of the system to industrial management. The industrial management structure was coterminal with the family structure. The managing agency system ensured the continuity of the hold of the family and its head on the industrial enterprises initiated by it. In addition, the duty of a son was to ensure the continuance of his inheritance for the future generations. Hence, unlike in the west where a child often rejects his father's operations, in India the son customarily obeys the father. This led to expansion of most ventures which the original entrepreneur left behind.

Referring to Chandler’s definition and reasons for the emergence of managerial class in America, one hypothesis can be suggested on the basis of the above. The managing agency system which became visible in the 1830's is evidence of a professional management cadre which lays claim to being known as India's managerial capitalism.

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